**IN THE HIGH COURT OF PUNJAB AND HARYANA AT CHANDIGARH**

****

**I.T.R. No.85 of 1987**
**Date of Decision:**

**The Commissioner of Income Tax, Patiala**
**.....Petitioner**

**Vs.**

**M/s Dev Raj & Sons, Chandigarh**
**.....Respondent**

**CORAM:- HON'BLE MR. JUSTICE ADARSH KUMAR GOEL**
**HON'BLE MR. JUSTICE RAJESH BINDAL**

Present:- Mr. S.K.Garg Narwana, Advocate for the revenue.

****

**ADARSH KUMAR GOEL, J.**

Following question of law has been referred for the opinion of this Court by the Income Tax Appellate Tribunal, Chandigarh Bench, Chandigarh (for short, `the Tribunal') arising out of its order dated 20.12.1985 in I.T.A. No.690/Chandi/84, for the assessment year 1981-82:-

> "Whether, on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in law in deleting an addition of Rs.45,000/- made on account of salary paid to the members of the assessee AOP?"

The registered firm was in existence in the name and style of the assessee prior to 2.4.1979 on which date, one of the partners expired and two of the partners disassociated themselves from the business and the remaining partners continued the business as joint owners without a fresh partnership deed. Dissolution agreement was signed between the parties w.e.f. 31.3.1980. During the relevant assessment year, the said three persons carried on the business of the firm and filed their return in the status of AOP which was accepted by the Assessing Officer. The assessee claimed salaries paid to its members, which was sought to be deducted out of total income. It was stated that for salary paid to the partners, there was a specific provision

under Section 40(b) of the Income Tax Act, 1961 (for short, `the Act') and payment of salary was not allowable but since such a provision did not exist in respect of AOP, payment of salary had to be allowed as necessary expenditure for carrying on business. This claim was rejected by the Assessing Officer, which view was also upheld by the appellate authority but on further appeal, the Tribunal upheld the claim. It was observed:-

> "We have given our careful consideration to the rival submissions. In our opinion, the assessee deserves to succeed. AOP is a separate and distinct entity from the individuals constituting it. It is separately assessable under the Income Tax Act. Employer and employee relationship in our opinion is not necessary for claiming salary. It is a matter of contract between the parties. We also agree with the learned counsel for the assessee that in case of the firm the salary allowedto the partners is as a result of the contract and the disallowance thereof is by the specific provisions of law being section 40(b) of the Income tax Act. There is no prohibition in respect of salary allowed to the members of an AOP. It can neither be said as a payment to self. We also notice that it was not the case of the ITO that no services were rendered by these members. It is only the AAC who introduced this aspect in his order. However, he has not brought any evidence on record to show that these persons did not render services. Neither there is any evidence on record to show that some outsider was managing the affairs of the assessee. The natural presumption, therefore, would be that the members rendered services for the running of the business. It can neither be said to be the diversion of profit as contended by the learned Departmental Representative. The learned counsel for the assessee has also spelt out the qualifications and experience of the members which have not been controverted by the learned Department representative. In such circumstances, we have no hesitation in holding that the observation by the AAC on this account are more surmises and conjectures. His order on this point is, therefore, reversed. The assessee will be entitled to deduction

of Rs.45,000/-. The ITO is directed to allow the same."

We find that the specific provision for disallowance of any payment of interest, salary, bonus, omission or remission made by association of persons to a member of such association or body was added in Section 40(b)(a) vide Direct Tax Laws (Amendment) Act, 1989 with effect from 1.4.1989. For the period prior thereto, there was no provision prohibiting such a disallowance. The assessment year involved in the present case being 1981-82, and there being no specific provision disallowing such a deduction, we are of the view that the findings recorded by the Tribunal are in conformity with the then existing law.

Accordingly, the question referred is answered against the Revenue and in favour of the asseseee. The reference is disposed of accordingly.

**( ADARSH KUMAR GOEL )**
**JUDGE**

**November , 2006** **( RAJESH BINDAL )**
**renu** **JUDGE**